RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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26 Letters Per Year • $250 annually

Sept. 27, 1995 **LETTER 1183**

Sept. 15 DJIA 4797.57; PTI 4284; A-D Ratio -2.64
Sept. 22 DJIA 4764.15; PTI 4282; A-D Ratio -3.21
Dow Yield: 2.42%; Dow Price/Earnings: 14.8
Dow 200-day MA: 4288; Dow 30-day MA: 4676
Dow Times Book Value: 3.64; PTI 89-day MA: 4205
Percentage of Undervalued Blue-chips: 5%
Gold 200-day MA: 384.51; Gold-PTI: 711

TRUE CONFESSIONS: They say that when you're over 70 (I'm referring to age, not height in inches) you can stop talking BS. When you're over 70, it's time to be honest. The secret is out: I'm over 70. Subscriptions here (surprisingly) continue to run at peak levels, this in the face of what has been described as one of the *worst periods for investment advisory publications in recent years.* And (being a wonderer) I've been wondering why business continues to be good here. Is there a catch?

My conclusion: I really do have serious subscribers (7,000 of them at present). I don't tout stocks when I don't love the market. I don't write about "Dow 10,000" just because I think it will sell. And I ask a load of questions, even if (damn it) I don't always have the answers.

Today, many investors have big paper profits in stocks and a lot of people are doing very well in business. BUT -- behind all this I sense a good deal of suspicion and worry. My subscribers are not stupid. They know that 2 plus 2 equals 4, not 5 or 6, as Washington would have us believe. They know this market is high, that it's rising parabolically -- and that it's vulnerable. They are aware that stocks are being touted from every quarter. But what really worries my subscribers is that they also know that as night follows day, bear markets follow bull markets.

The truth -- I'm struggling with most of the same questions my subscribers are struggling with. Veteran investors know only too well that nobody has the final answers in this business, at least not for long. Or as I've often put it, *"There are no geniuses on Wall Street, only geniuses for a while."* At any rate, all I can promise is to do my best in this strange "market-mania" atmosphere of the mid-'90s.

THE PICTURE: Every once in a while we will witness a market move (an advance or a decline) that *goes further than anyone believes possible.* Obviously we've been seeing just that kind of phenomenon in the US stock market.

Back in 1974, with the Dow at 577.60, I sent out a "Special Report" (mailed on December 19, 1974). In that report I opined that the great bear market was over and that a new bull market was in the process of being born. Consequently, I recommended buying, and I provided a list of stocks to buy.

However, I would have been absolutely flabbergasted at that time if you had told me that 21 years later the Dow would rise to a price of over 4800. As for the Rail Average (now called the Transportation Average), which in '74 had collapsed to 125.93, never in my wildest dreams did I think that lowly Average would climb to over 2000 during 1995. As for the Utility Average which had smashed to a 1974 low of 57.93, that Average rose to a high of 256.46 in 1993. Of course, it hasn't been higher since (and that's a cause for worry).

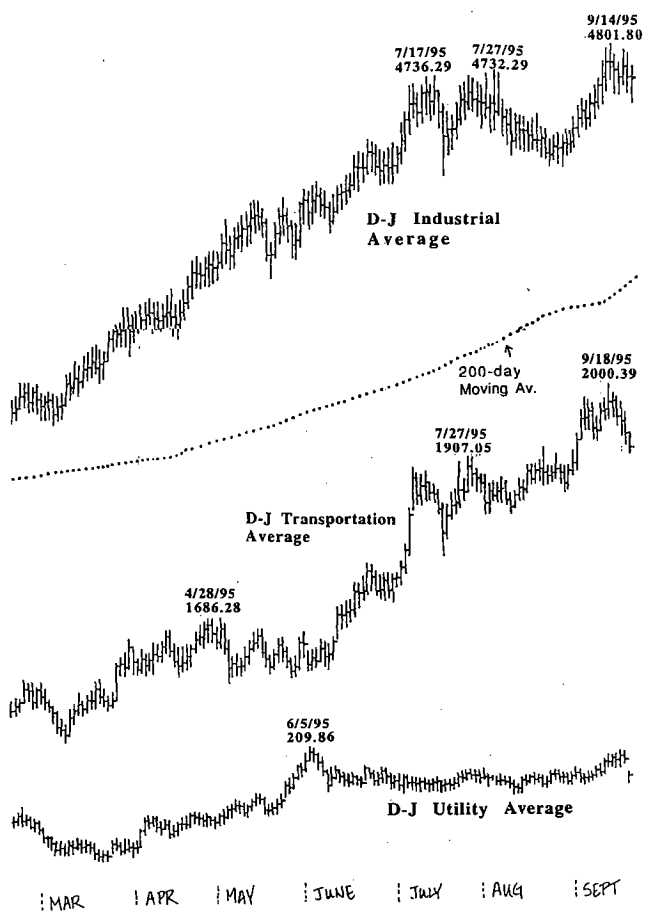
All right, let's talk about the present. This is a bull market that has obviously enjoyed shocking us on the upside. On September 12 the Dow advanced to a closing high of 4747.21, thereby bettering its July 17 high and finally confirming the series of new highs in the Transportation Average.

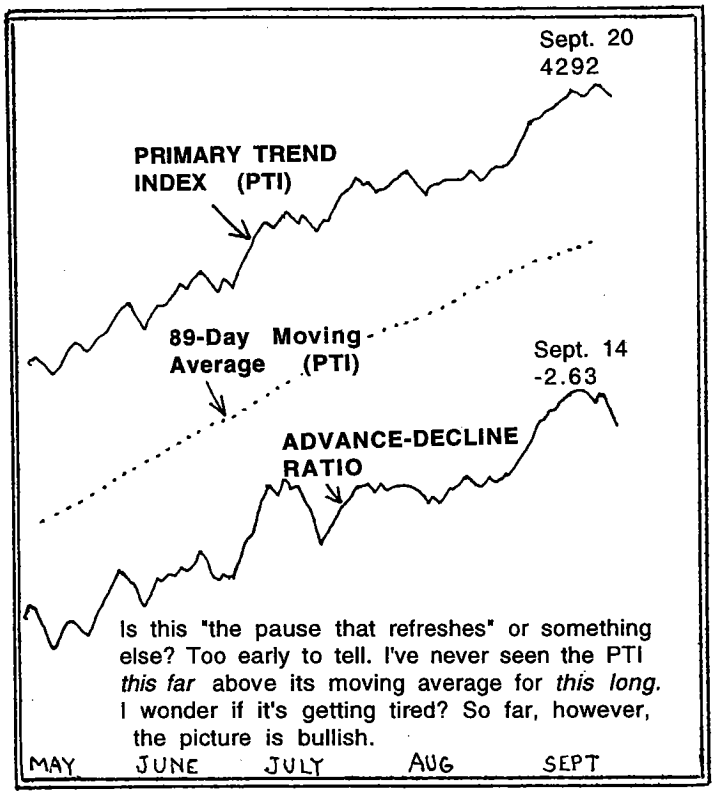
From there on it's been an upside see-saw, with first one Average, then the other, rallying to record highs. Daily new highs (individual stocks) on the NYSE have generally remained at the over-200 level. Market action has been firm, and you get the feeling that there'll never be another correction, much less a bear market. Time after time the market will open down and then spend the rest of the day pushing north, only to close the day on the upside. It's eerie. It's uncanny. You can almost write a song about it -- "It's the Market That Will Never Go Down" (music by R. Russell).

Each bull market differs from every other bull market in numerous ways, but all bull markets possess one thing in common. That one thing is (dare I let the secret out) *more buyers than sellers.* In this bull market, at least since 1994, we've had literally nothing but buyers with an obvious dearth of sellers.

The question: what has made this bull market different? As I see it, the big difference in this bull market is the *rise of mutual funds and the all-out acceptance of the funds by the public.* Today there are an absurd total of over 5,000 equity mutual funds, all of them vying to "beat the averages" and all of them competing with each other.

The Operative Thesis: The primary trend of the market is *bullish.* And we'll continue to classify it as bullish until it is *proved*





otherwise. To me, the concept of the primary trend is the single most important and fascinating fact of this business. People ask me when I think this market will top out or how far I think the Dow can advance. I tell them that the market will continue to record new highs as long, and only as long, as the primary trend remains bullish. We may get declines, we may get temporary interruptions, we may even get full secondary reactions, but as long as the primary trend remains bullish, each and every retreat will be followed by new highs.

At some point (and we will probably be *unaware* of the exact day or even the week when this occurs) the primary trend of the stock market will turn bearish. When that happens the market will head down with each low ending *below* the last low and each rally peak terminating *below* the previous rally peak. But wait -- let's not jump the gun, let's deal with the fact of an aging yet still very much alive bull market.

Tactics: Since this advance, in terms of persistence and absence of correction, is almost unique, I continue to suggest that subscribers depend increasingly on my Primary Trend Index (PTI).

A recent subscriber asked me exactly what the PTI consists of and how it is calculated. I told him that the PTI is the only "secret" I have in this business. I told him that the PTI is composed of eight different indices and averages, each based entirely on market action. The reason I have never disclosed the makeup of the PTI is simple enough -- I'm afraid that if its composition and construction became public knowledge, the PTI would lose its effectiveness. "Too many cooks spoil the broth," and in this business, too many investors following an indicator usually renders that indicator useless (old timers probably remember what happened to the odd lots, the short interest, "will-go," the "Confidence Index" and many other so-called market guides).

Old Friend Joe Granville lists a number of distribution phenomena which occur at or near market tops: (1) Corporate mergers. (2) Raised dividends. (3) Stock splits. And as further indications of distribution -- (4) Secondary offerings. (5) Insider selling. Remember, big (smart) money doesn't sell stocks on bad news, no, it sells stocks with the help of good news and rosy predictions (speaking of distribution, how about that Telephone breakup!).

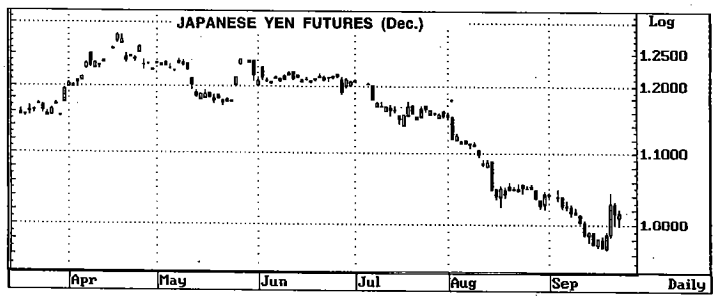
Strange: *Investment Quality Trends* here in La Jolla closely monitors 350 blue-chip stocks. In their latest report they write that in August 1987 (the peak then just before the crash) 42 stocks or 12% of their universe were in Declining Trends. Then they note that at the beginning of September 1995 120 or 35% of the stocks they monitor were in Declining Trends. They conclude, "There are three times as many stocks in Declining Trends now as there were at the market peak in 1987." **Russell comment:** Go figure!

INVESTMENT POSITION: The bull remains in the box. This is an aged bull, he's a bit short on breath, but he's still on his feet, and that's what counts with bulls.

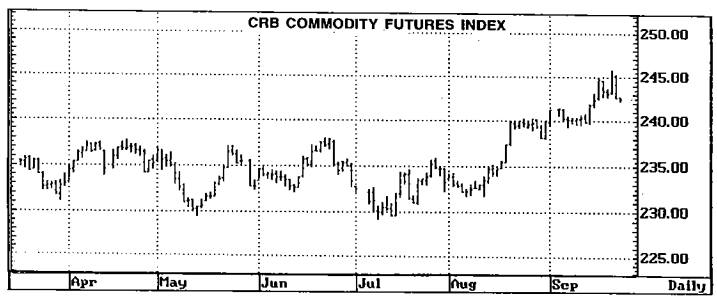
Personally, I'm a little worried about this stock market. And to tell the truth, I'm not even in love with the bond market. Right now I'd rather be where no one else is. Let's see -- where could that be? Oh yeah, I think it's in cash. Margin debt is high, consumer debt is high, the US government will be faced in a few weeks with having to raise the national debt to over $5 trillion. Everybody, it seems, owes lots of money. But that's OK because it's a bull market, isn't it? Gosh, I really feel like an idiot being liquid and all, and not owing anyone anything.

Well, read the gold section and you'll get a better idea of my attitude.

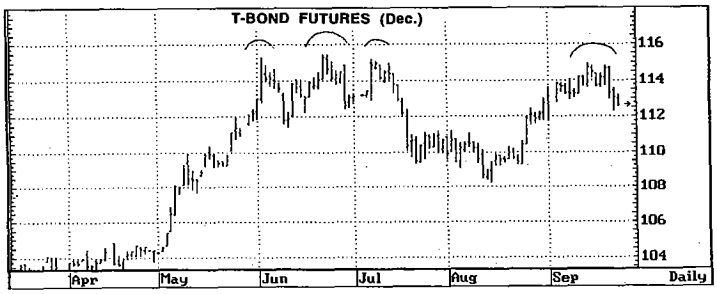
CHARTS: Following are a few charts worth studying. The first chart is one I guess we could call the chart of the month or even THE chart of 1995. It shows the huge (25% in five months) plunge of the Japanese yen against the dollar. The US trade balance was at a negative record last month. I can't imagine that this month's considerably stronger dollar will help the trade balance any (remember, a stronger dollar means higher prices for US exports and lower prices for Japanese exports).



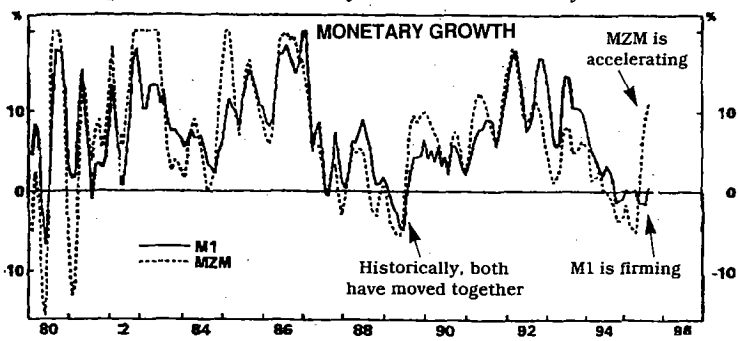
Next, the CRB Commodity Futures; here we see the bullish breakout above 230 and the subsequent climb. The impetus behind this move is mostly the strength in the grains. The world grain stock has dropped dangerously low. Cotton, corn, wheat, soy beans, the prices are all exploding.



The third chart shows the Treasury Bond Futures contract. The bonds made a triple top during June and July in the 115-116, then rallied this month back to the 115 level. There's obviously huge resistance at around 115. T'will be interesting to see whether the bonds can get above 115 (I don't think they'll make it).



The last chart shows monetary growth with MZM (money of zero maturity) accelerating to the upside. Ed Hyman considers MZM one of the best measurements of money. At any rate, it looks like the Fed is jazzing up the money supply, preparatory to the coming election (and remember, Greenspan wants to be reappointed to the Fed head position). Chart courtesy of *Bank Credit Analyst.*



CAPITAL: Following is a simple but critical thesis that I would like all my subscribers to understand (wealthy ones already do). There's a **vast difference** between your capital and your interest income or your dividends. Here's the difference. Your capital is the savings that you have accumulated after all your hard work and after paying all the various taxes. Therefore, your capital must be respected. Your capital represents the tools of your trade and, of course, your trade, in this case, is the investing business.

Your income can be salary, interest, dividends, rental income, etc. It's whatever money your capital or your investments or your business brings in.

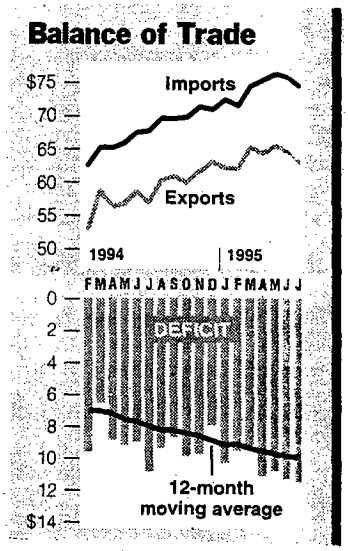
I have five children (four are grown up now), and where finance is concerned, the one thing I drill into their heads is that you do not spend your capital. If you must spend more than the regular income or salary that you receive from your job -- then turn to your other income (dividends, interest, etc.). But again, DO NOT SPEND YOUR CAPITAL.

Capital, if correctly and intelligently positioned, increases itself. But all too often people spend their capital or deplete it in some wildly speculative or senseless scheme, a scheme that results in a major loss. I tell my kids that under today's confiscatory tax system, capital is extremely difficult to accumulate. As such, it must be respected. But all too often, people (particularly if it's inherited) treat their capital like a one-shot gift.

To my mind, the weakness in mutual funds is that fund managers are not dealing with their own money, their own capital. Thus, mutual fund managers do not respect the money they handle as much as they respect their own money. Of course, you can't blame them for that -- it's just human nature. (In actual fact, many fund managers keep most of their own money in T-bills.)

As a fund manager, when the fund you manage drops 40% in a major bear market, it hurts. You feel bad. You screwed up, and you may even have to look for another job. But when you own account drops 40%, you can't sleep, you torture yourself because you were so stupid, you feel sick, you curse the market, you hate Wall Street -- you swear that you'll "never buy another stock again."

So treat your capital with respect. It can be your friend and helper for life, or it can be the friend you lost and wish you still had. And remember that deadly formula -- if you have $50,000 and you lose $25,000, you've lost half your money and you're down 50%. But to bring your $25,000 back to $50,000 again, you have to make 100% after taxes. And brother, that's just not easy.



NOTES & QUOTES: For years Washington has been complaining about our trade "imbalance" with Japan. But the latest July trade figures show a new record deficit -- and this with our trade deficit with Japan having actually improved! But our trade deficit with Taiwan, Singapore, S. Korea and Hong Kong soared $1 billion (some think this merely represents a shift of Japanese production to other Asia countries). The problem is basic: US exports can't keep up with US imports. At the current rate, the trade balance is going to be a negative $130 to $140 billion. That's a lot of dollars going overseas. As to the $1 billion a day in federal deficits, much of it is financed by foreign buyers, and you get a picture of the long-term pressure on the dollar.

* *

Synergy -- That's the buzz word behind all the recent mergers, particularly in the entertainment industry. So Wall Street gasped (but liked it) when AT&T announced that it was breaking up into three separate corporations; "reverse-synergy," I call it. It also makes me wonder whether combinations such as Disney and Cap/ABC are going to work out. Or whether we're going to see reverse-synergy as the wave of the future.

* *

Perhaps the biggest shock and danger confronting Americans is the coming meltdown in **unfunded liabilities.** Two excellent books have come out dealing with this explosive subject. One is the hard cover book by Craig Karpell (Harper Collins) entitled, *"The Retirement Myth, What You Must Know to Prosper in the Coming Meltdown of Job Security, Pension Plans, Social Security, the Stock Market, Housing Prices."* The other book (author is Ron Holland) is paper bound and is entitled *"Escape the Pension Trap, What Will You Do When Your Retirement Plan Assets Are Taxed & Plundered to Generate Revenue for a Desperate Federal Government?"* Both of these books (with flagrant titles) are well worth reading and should be taken seriously. The first can be purchased at your local bookstore. The Holland book costs $20; write to Offshore Publications, PO Box 1201, Skyland, NC 28776. The first chapter of the Holland book is entitled, "The Target, Four Trillion in Retirement Funds." It starts, "Social Security is heading towards bankruptcy. The only actions that will save it are drastically reduced benefit payments and greatly increased SS taxes. The scale of benefit reductions and tax increases which will be required to head off this crisis are unprecedented in American history. What's more, the aging of the American population will result in too few working Americans to fund our 'safety net' of social programs. When these demographics are combined with our exploding national debt and a wasteful non-productive bureaucracy, the revenue costs of a government we don't need and can no longer afford becomes insurmountable . . . While there is much talk in Washington about the need to reduce government controls, services and expenses, I don't believe our Washington politicians of either party will do anything to bring any real reductions about." **Russell comment:** As I said, these two books are well worth reading in that they deal with the massive built-in problem of unfunded liabilities. These are problems that the politicians won't deal with honestly in their frantic haste to collect votes by "giving the people what they want." **Warning** -- The government tax-collectors are most apt to go after *where the money*

is or to the areas where the government loses the most. The leading areas of *revenue loss* by the government are: (1) Pensions where net exclusions run to $51.2 billion a year. (2) Mortgage deductions which run to $40.5 billion a year. (3) Employer contributions for medical insurance premiums and medical care which cost the government $33.5 billion. Watch these areas for the next IRS "hits."

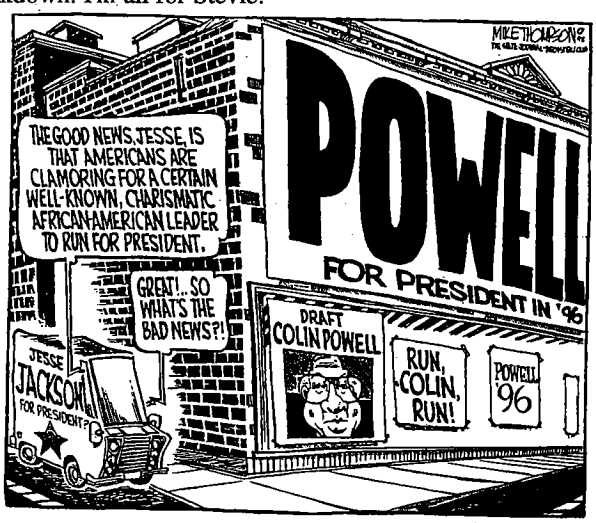
* *

I just received an ad in the mail from a fellow market-letter writer. The ad screams, "Clinton is on his way to making the comeback of the century in '96 . . . Gingrich and his Republican majority were elected on a promise to cut regulations, reduce the budget, and roll back taxes. Yet, at the end of their vaunted 100 days, not one regulation has been repealed, not one dime of spending reduced, and not one tax has been cut." **Russell comment:** Stinging words. And you know something -- this guy could be right. The key will be whether Clinton uses his veto power big time -- and if he does, how the voters take it.

* *

William Safire in the Sept. 11 *NY Times* opines that Colin Powell would be crazy to go for a third political party. If Powell is serious (and when he's finished going for the big money via his new book), then let him join one of the two leading political parties. Safire notes that the timid Powell was one of those who counseled Bush not to go the whole route and get rid of Saddam. Safire notes that Powell is "the man who had to be dragged into stopping Saddam Hussein" and he's also "the man who let the Republican guard escape because he didn't want to seem cruel on TV." Powell also warned Bush not to go into Panama and rid the nation of Noriega. Unlike Powell and Bradley, says Safire, Bill Clinton has "fire in his belly," Clinton is a tough campaigner while Powell would be "Candidate Feelgood." **Russell opinion:** I've watched Powell on TV. This guy is articulate, feels "safe," and is very reluctant to take strong positions. You can see why Powell rose to the top in the military; he's careful, careful, safe, smart, political. Powell is extremely popular with the people and is drawing big crowds on his lecture tour. However, I think he's totally status quo. My own favorite ticket would be President "Steve" Forbes (for brains) and Vice President Powell (for votes and popular appeal). But Powell says he's not interested in VP.

Steve Forbes? He's definitely running, and he's willing to spend $25 million of his own money on his campaign. His basic program -- a 17% flat tax and a return to the gold standard. Those two are enough to give the Washington establishment a nervous breakdown. I'm all for Stevie.


MIKE THOMPSON
THE GOOD NEWS, JESSE, IS THAT AMERICANS ARE CLAMORING FOR A CERTAIN WELL-KNOWN, CHARISMATIC AFRICAN-AMERICAN LEADER TO RUN FOR PRESIDENT.
GREAT!.. SO WHAT'S THE BAD NEWS?!
POWELL
FOR PRESIDENT IN '96
DRAFT COLIN POWELL
RUN, COLIN, RUN!
POWELL '96
JESSE JACKSON FOR PRESIDENT

* *

Nicholas Leeson is the trader (based in Singapore) who literally broke the venerable 232-year old Barings PLC bank. Leeson says that in a single day he was able to make or lose over $50 million. What was so shocking is that Leeson's superiors in London had no idea what the hell he was doing. Said Leeson, "It was advantageous to me that the people, the senior people in London that were arranging these payments, didn't understand the basic administration of futures and options, and that was probably the biggest failing; they wanted to believe." To Leeson's amazement, the London office kept sending him huge amounts of money daily, ultimately $1 billion more than the bank was worth. Leeson added, "It wasn't fun at all, I hated every minute of it. I mean, you know, I was looking at massive figures; masses losses every day . . . I was hiding from the figures, I was in a situation where I wasn't asking for the balance. It scared me to death, and I just didn't want to know . . . It was the scariest thing in my life." **Russell comment:** When you trade options or futures or currencies, you better darn well mark to market not daily but hourly. Once you let your trades get away from you, you're in major trouble. Remember the old adage, "it's no sin to be wrong -- the cardinal sin is to STAY wrong." Neither Citron of Orange Country nor Leeson of Barings monitored their huge positions on a mark to market basis, and when their positions went against them they first panicked, then they froze. And their supervisors didn't know what was going on.

* *

The Japanese government is now frantic to reinflate their deflating economy. Their central bank (Bank of Japan) has brought the discount rate down to 0.6% while the banks can lend at 2-3%. This, they hope, will allow the banks to reliquefy (as per the US banks during the '90s). Japanese banks are loaded with more than $600 billion in bad debts, which is roughly twice the problem that the US S&L industry had to deal with. Japanese real estate prices have collapsed, and the yen has plunged against the dollar. Will Japan be able to reliquefy and turn the corner? Their Nikkei stock average suggests that the answer is "probably," since it has now recorded a double bottom at the '92 and '95 lows and has now rallied from the 14,000 area to the 18,000 area.

* *

Gordon Moore is one of the co-founders of Intel, the computer chip company (sales $16 billion) that is probably the microprocessor leader of the world. In a fascinating *Forbes* interview Moore said, "One day, *Forbes* will be able to simultaneously publish the magazine in 50 different languages simply by pushing a button . . . More educated people who can use computers are going to do better than poorly educated persons who are technically illiterate. I'm worried already that we've taken a big step towards being a two-class society based on education. The personal computer will facilitate the upwardly mobile. The educated classes will turn in their computers every few years just to get the more powerful version." *Forbes* notes that "already the computer has started to make obsolete certain professions. Intel has already gotten rid of many of its secretaries. Fewer librarians will be needed. The same with paralegals and all manners of clerks." About the Internet? Moore said that "it supplies less than 1% of the information in the world now. It is just one step towards the global electronic library." Asked which companies will be the future winners, Moore said, "I consider it group grope. I wouldn't be surprised if the eventual big players were companies that we've never heard of at this stage of the game." Moore expects the semiconductor industry to grow until it reaches 1% of the world economy.

* *

Recession coming? No way. Two leading economic forecasting organizations say a recession is unlikely this year or even next. The National Association of Business Economists and Blue Chip Economic Indicators believe that the economy will grow by 2.9% this year and 2.4% next year. Not one of the 52 forecasters in the Blue Chip poll thought a recession was likely this year or next. The two polls produced identical predictions for inflation: 3% this year and 3.2% in '96. **Russell comment:** If you're a contrarian, I guess you can start to batten the hatches. Of the 101 economists questioned in both polls, only one person saw a recession beginning this year.

* *

What Next? *USA Today* has introduced a new monthly feature; they will review a reader's mutual fund portfolio and "recommend improvements." Note on this clip that mutual funds are equated with the idea of "a cozy retirement." Have common stocks and mutual funds ever been this accepted as the royal road to health and happiness? The Sept. 18 *WSJ* features a front page piece which talks about many individuals now starting their own mutual funds. It's an epidemic, based on the public's willingness to throw money at anything having to do with Wall Street. Talk about manias!

USA TODAY • TUESDAY, SEPTEMBER 5, 1995 • 3B

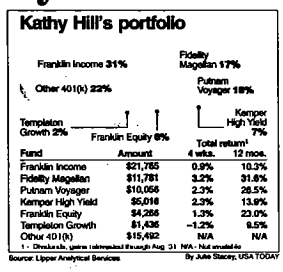
MANAGING YOUR MONEY

Each month, an investment expert reviews a reader's mutual fund portfolio and recommends improvements.

Late bloomer plans cozy retirement

Kathy Hill got a late start on her career as a flight attendant -- and on her investments. Hill, 45, a single mother who lives in suburban Minneapolis with her two children, began flying 10 years ago after her marriage ended in divorce. "It's something I always wanted to do," she says.

Kathy Hill's portfolio



Fund	Amount	Total return[1] 4 wks.	12 mos.
Franklin Income	$21,765	0.9%	10.3%
Fidelity Magellan	$11,781	3.2%	31.6%
Putnam Voyager	$10,056	2.3%	26.5%
Kemper High Yield	$5,018	2.3%	13.9%
Franklin Equity	$4,256	1.3%	22.0%
Templeton Growth	$1,436	-1.2%	8.5%
Other 401(k)	$15,492	N/A	N/A

1 - Dividends, gains reinvested through Aug. 31 N/A - Not available

Source: Lipper Analytical Services

By Julie Stacey, USA TODAY

* *

My old friend, Bob Prechter (*"Elliott Wave Theorist"*) has just published the ultimate bear market book, a hard-cover volume entitled, *"At the Crest of the Tidal Wave, A Forecast for the Great Bear Market."* The book is thoroughly interesting, not only for its technical analyses but for its social commentaries (Prechter is a brilliant observer of our society and its culture and its changes). Sample technical comment: Prechter talks about the historic low volatility of the stock market since 1992. "The entire span of the past three to four years, then, is setting an all-time record (perhaps for any stock market ever) for its dearth of price-related psychological upset near an all-time high. What explains these phenomena? The lack of volatility in today's market is both an *effect* of the bull's complacency and a *cause* for further complacency. The market's calm is widely presumed to be 'normal' when, in fact, it is so abnormal *that it is unprecedented.*. Such long periods of uncorrected advance do not suggest that 'a 10% correction is due'. They reveal deep investor complacency and therefore market tops, which is why they have preceded major downside reversals. The next 10 years will witness volatility equal to or greater than that during 1931 to 1933 and shake investors out of their carefree dream world for many decades." To order this fascinating book call (800)336-1618. **Russell comment:** The calm comes before the storm. Out of this period of unprecedented LOW volatility we will experience a period of HIGH volatility. I'd be willing to bet that the high volatility will be on the downside.

* *

Booming China: This from a San Diego lawyer just back from a trip to China: "Joint ventures are sweeping China -- there are 70,000 joint ventures going on in Beijing alone . . . A vast difference in level of development in different cities. In Beijing they are enthralled with the FAX machine, but had little understanding of computers, much less of modems and the Internet; in Hangzhou they are just learning about computer technology, but are not yet working with database programs; in Shanghai, however, they have a vast network of computer programs." In a vocations/technical school in Shanghai "it was interesting to see the computers equipped with software which translates the English keyboard into Chinese characters . . . Coca Cola was everywhere we went! . . . Another fact that emerged as we met with different labor departments is that for every job application in China, there are six job openings. It seems inconceivable in a country of so many people that they cannot find enough people to fill waiting jobs . . . Everywhere we passed had the appearance of just coming out of a war -- piles of rubble and brick everywhere. The amount of building going on is staggering . . . in Shanghai alone there were four high-rise buildings being constructed across the street from our hotel. We dubbed the building crane as the new national bird of China! Their scaffolding is almost exclusively made of bamboo poles and wire. And every building we saw had a definite design--no four-sided skyscrapers for the Chinese! . . . It is true one cannot drink the water in China, but bottled water is provided everywhere, including at the sink in hotel rooms. There seemed to be no shortage of food in China. On almost every street corner food was either being sold or cooked. And many of their 'delicacies' which we sampled continue to this day to be 'mystery meat'."

* *

Enter #5: Well, my fifth grandchild just arrived, courtesy of daughter Betsy out of LA. This one's a boy and his name is a mouthful -- Vincent Russell Van Patten, Jr. His big brother, Duke Van Patten (age two-and-a-half), is already swinging a tennis racket as per his dad. Betsy also tells me that "this is it --two is enough."

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I took the Amtrak round-trip to LA. Cost (senior discount) round trip, San Diego to LA and back, was an amazingly low $32. The train was spotless and comfortable -- coffee, O. J., hot chocolate and newspapers were free. In all, I was impressed -- this may be the biggest bargain since the Paramount's early show -- Frank Sinatra with Tommy Dorsey's band plus a new movie, all for 75 cents before noon (44th at B'way, hey, is the Paramount still there?).

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The Sept. 9 issue of the *Economist* features "The Disappearing Family." Writes the *Economist,* "In America, families are valued tremendously -- so much so that most people will have at least two of them. Americans are religious, but have one of the highest divorce rates in the world. They are ambivalent about abortions but have lots of them. Government has worked hard to make public policy as contradictory as private choices. There is a marriage penalty at the middle to upper end of the income-tax schedule; married couples pay more tax than two single people with the same income . . . Divorce is easy. Three out of 10 American children will sleep in a different home than their father tonight. Among black children the rate is six out of 10 . . . The welfare check, with its attendant medical benefits and food stamps, became considerably more valuable to have than a low-wage husband or father. Half a million teenagers have babies every year; very few of them go home to their father. More than half the 5 million women on welfare started as teen-age mothers. Their daughters will follow their mother's footsteps; their sons often follow in their fathers'." **Russell comment:** I blame a good part of this social mess on the welfare state, which has gone a long way towards undermining individual responsibility.

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The Sept. 25 *Forbes* contains an article about the new book, "The End of Racism," by Dinesh D'Souza. The book delves into the problem of America's blacks. Says D'Souza, "Much of black American culture is simply dysfunctional. It is this that causes many of the problems conventionally blamed on 'racism'." D'Souza cites black educational under performance at every level. This, he argues, must be related to the widespread repudiation of academic achievement and even standard English is seen as 'acting white' (some inner-city school children are now being taught to count in Swahili). High illegitimacy rates and stunning levels of violence (in 1992 half of US murder victims were black, 94% killed by other blacks) don't help either." **Russell comment:** With it all, the Hispanic rate of high-school dropouts is far higher than the black rate. American society in general is becoming dysfunctional. If history is any guide, there will ultimately be a fierce back-lash against the super-liberal state (I think it's already happening, but in a small way).

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Visitors to my office or house ask me why I read a number of right-wing publications. I tell them that these newspapers and magazines are simply an antidote to the well-known national publications that I receive. Almost all the big-circulation newspapers and most of the national magazines vary from liberal to extremely liberal. To tune in to the conservative side of the story you might want to subscribe to *Human Events* -- (800)787-7557 or *The Washington Times* -- (800)363-9118 or *The Conservative Chronicle* (many top columns) -- (800)888-3039.

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Shocking words? This from a Thomas Friedman editorial in the Sept. 18 *NY Times:* "While the Clinton administration is working and praying for Saddam's demise, most of his fellow rulers like him just the way he is. That is, strong enough to hold Iraq together, weak enough not to threaten his neighbors, embargoed enough not to be able to sell too much oil and caged enough not to be a factor in inter-Arab politics. This is a Saddam that serves a lot of people's interests, and the Clinton administration is fooling itself in thinking otherwise.

GOLD, JAPAN AND MONEY: What's happening in Japan today is extremely significant, and it may provide a scenario for what lies ahead for us in the future. Japan is suffering a massive deflation. Real estate and land prices have dropped as much as 50%. Japanese banks, heavily invested in real estate, are struggling with over $600 billion in bad loans. Japanese workers, for the first time since World War II, are being laid off, and Japanese investors are bailing out of costly overseas investments (two weeks ago mighty Mitsubishi walked away from a $2 billion investment -- Rockefeller Center -- a loan that went bad). The reaction by the Bank of Japan to the deflationary recession has been to rush to reinflate, to print money, to drop interest rates to well below 1%, to buy dollars and intervene to boost the dollar and knock the yen down, to do whatever they have to -- to reinflate the sagging Japanese economic balloon.

As a result of the flood of yen, the price of the yen vs. the dollar has dropped. In the last two months alone the yen has declined over 20% against the dollar. Flooding the market with yen has brought the Bank of Japan and Japanese businessmen some of the results they wanted -- which is a *much cheaper yen plus the much-desired export advantage.*

In the face of all this, gold has reversed its long down-trend against the yen. Gold has been moving up against the yen. But gold in terms of dollars has done little. However, I notice an unusual phenomenon. During the first half of 1995 gold usage (mostly for jewelry) has increased to record levels. I notice something else -- gem quality stones -- diamonds, rubies, emeralds, sapphires have been bringing fat prices. Quality gems represent one of the few accepted types of *portable wealth,* and it's obvious that someone or somebody has been taking high-quality gems off the market, in many cases at record prices.

So I ask myself -- "Russell, what will happen when the inevitable finally occurs? What will happen when, following this explosive, parabolic rise in stocks, the primary trend turns down and a bear market takes over? What will happen when US stocks collapse and when the economy follows stocks down?"

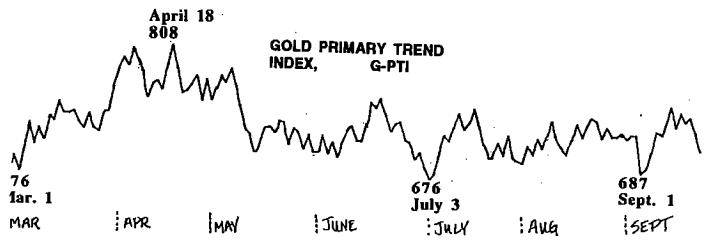
The answer is obvious, at least it is to me. The answer is that the Fed will fight the downtrend with all the weapons at its command. The Fed will do exactly what the bank of Japan is now doing, which entails *flooding the banks and the nation with liquidity.* That process will drive the dollar down, rendering US goods cheaper compared with goods in the rest of the world. But with a bear market in force, other nations are hardly likely to sit back and allow the US to enjoy the cheap currency advantage. No, there will be competitive devaluations as the central banks of the world each move to cheapen their currencies and give their respective economies the export advantage.

This is the point where I believe we will see the makings of a big bull market in gold. But today gold is cheap, and consciously or unconsciously, people sense it. That is why so much gold is being bought in record quantities at today's "bargain prices." And that, I believe, is why portable wealth in the form of precious gems is also being bought up and locked away even at today's high prices for jewelry.

Let's face it, following an initial deflation, the Fed will step in, and the purchasing power of the dollar could easily be halved during the next bear market. But gold is still gold and a ruby is still a ruby and a diamond is still a diamond, and all three will be objects of value 100 years from now when paper dollars are just a distant memory.

So we can and should learn from what's happening in Japan today. Politically, nations will no longer stand still when their economies deflate. No, nations will fight deflation as Japan is now fighting -- by literally printing money and flooding their respective nations with liquidity.

In the meantime, my Gold Primary Trend Index (G-PTI) shows an extended period of indecisiveness, with the G-PTI simply fluctuating aimlessly with every up-tick or down-tick in the metal.



LATE NOTES: Let's face it, the Republicans haven't done well, so far, in converting their "Contract With America" into law. They just haven't done anything to make US voters say, "Wow, these guys have brought in change; they're getting it done." In desperation the Republicans are ready (so says Newt) to play hard ball. The GOP will refuse to vote to raise our insane national debt to above the $5 trillion -- unless Bill Clinton goes along with their program (welfare, tax changes and all the rest).

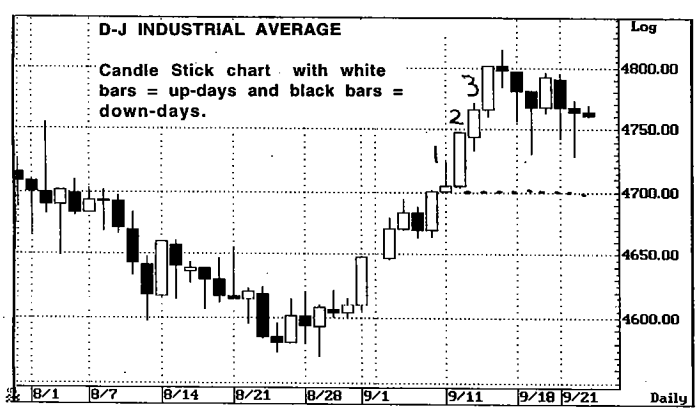
Is this just another idle threat? In the past when this same threat arose, a last-minute cave-in has always occurred, and trouble has been avoided. But as I say, the Republicans are now desperate to get something done. If they don't, the Contract With America is going to look increasingly like another political bad joke.

Weakness: The stock market's been weak lately, ostensibly because of the weak dollar plus the possibility of a government shutdown. But listen, pros don't sell stocks based on potential temporary trouble. And even if the Republican threat does come to pass and the government actually is shut down, how long would it remain down? A few days? A week? Big deal.

Nasty thought: Now if the bear really wanted to be nasty, here's what he could do. He could actually materialize -- in other words, a primary bear market could start here. But if a bear market did start, everybody would think that it was merely the weak dollar or the trouble in Washington that was the cause. Nobody would believe that a true primary bear market was underway. Just a thought, dear subscribers, just a thought.

The chart below is a Japanese candle stick chart of the daily Dow (white bars are up-days, black are down-days). The technique I use to read these charts is that a true or important reversal entails a *wipe out of the advance or decline of the three previous up or down days.* In this instance I have labeled the three previous up-days with a 1, 2 and 3. For a candle stick reversal, the Dow would have to break below #1, which would mean a Dow closing below **4700.** A Dow below 4700 would be the first sign of true market weakness. Barring a violation of Dow 4700, I would not be impressed with the downside in this market.

As this is written, I continue to get the feeling that the funds and investors just can't wait to buy this market on any slight sign of weakness.



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